

Message Text

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FM AMEMBASSY MANILA

TO SECSTATE WASHDC 3031

UNCLAS SECTION 1 OF 2 MANILA 3632/1

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TAGS: AFIN, RP

SUBJ: CANADA AND PHILIPPINES SIGN TAX TREATY

REF: STATE 61418 (NOTAL)

1. LARGE OFFICIAL CANADIAN TRADE DELEGATION HEADED BY DONALD JAMIESON, MINISTER FOR TRADE, COMMERCE, AND INDUSTRY, VISITED MANILA MARCH 11 AND 12. ONE OF PRINCIPAL ACCOMPLISHMENTS WAS SIGNATURE MARCH 11 OF TAXATION TREATY. EMBASSY IS SEEKING TO OBTAIN COPY. IN MEANTIME, DEPARTMENT AND TREASURY MAY FIND OF INTEREST FOLLOWING STORY FROM MANILA DAILY E "BUSINESS DAY" WHICH DESCRIBES SEVERAL FEATURES OF THE TREATY:

QUOTE THE PHILIPPINES AND CANADA YESTERDAY SIGNED A TAX TREATY, WHICH IS EXPECTED TO PROMOTE INTERNATIONAL TRADE AND INVESTMENT IN BOTH COUNTRIES AND ALSO TO IMPROVE TAX EQUITY THROUGH THE ELIMINATION OF DOUBLE TAXATION AND THE PREVENTION OF TAX EVASION.

THE TREATY, SIGNED BY PHILIPPINE FINANCE SECRETARY CESAR VIRATA AND CANADIAN MINISTER DONALD JAMIESON OF THE MINISTRY OF TRADE, COMMERCE, AND INDUSTRY, ESTABLISHED RULES AS TO SOURCE, RESIDENCE AND TAX TREATMENT OF SPECIFIC TYPES OF INCOME TO REMOVE PROBLEMS RESULTING FROM INTERNATIONAL TRANSACTIONS, SUCH AS FOREIGN INVESTMENTS.

A PROVISION OF THE TREATY GIVES THE PHILIPPINES THE RIGHT TO TAX FILIPINO CITIZENS RESIDING IN CANADA WITH A

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CONDITION THAT THE TOTAL TAX LIABILITY OF SUCH CITIZENS

WOULD NOT BE MORE THAN THE TOTAL PHILIPPINE TAX IF THEY WERE RESIDING IN THE PHILIPPINES.

CANADA ALSO ACCEDED TO AN AIRLINE AND SHIPPING TAX FORMULA OF 2.5 PER CENT INCOME TAX ON GROSS BILLINGS FROM PHILIPPINE SOURCES ON AN MFN (MOST-FAVORED-NATION) BASIS.

"FORCE OF ATTRACTION" BOTH COUNTRIES ALSO ADOPTED THE "FORCE OF ATTRACTION" RULE WHEREBY A PERMANENT ESTABLISHMENT CAN BE HELD LIABLE TO PHILIPPINE TAXATION IF CERTAIN ACTIVITIES ARE RESORTED TO FOR MINIMIZING DECLARATION OF ATTRIBUTABLE INCOME.

BOTH COUNTRIES ENLARGED THE DEFINITION OF PERMENENT ESTABLISHMENT TO INCLUDE INSURANCE ACTIVITES FOR A BUILDING, CONSTRCTION OR ASSEMBLY PROJECT. ANOTHER FEATURE OF THE TREATY IS CANADA'S CONSENT TO GIVE THE PHILIPPINES A TAX SPARING CREDIT FOR THE AMOUNT OF TAXES REDUCED UNDER THIS TREATY. THIS PROVISION IN THE TREATY FAVORS CANADIAN INVESTORS IN PORTFOLIO THE TREATY FAVORS CANADIAN INVESTORS IN PORTFOLIO INVESTMENTS.

BOTH COUNTRIES ALSO ESTABLISHED A CONSULATIVE MECHANISM BETWEEN THE TWO TAX ADMINISTRATIONS FOR IMPLEMENTING THE PROVISIONS OF THE TREATY AND FOR STABLIZING THE TAX RULES THAT ACCOMPANY SUCH AN AGREEMENT.

THE PHILIPPINES AND CANADA ALSO AGREED TO EXCHANGE INFORMATION FOR PREVENTING FRAUD OR FISCAL EVASION.

THE TREATY IS THE FOURTH TO BE ENTERED IN BY THE PHILIPPINES WITH FOREIGN GOVERNMENTS. PREVIOUS TAX TREATIES WERE WITH SWEDEN, DENMARK AND FRANCE. OTHER TAX TREATIES UNDER NEGOTIATION ARE THE NORWAY, THE UNITED STATES, BELGIUM, THE NETHERLANDS, WEST GERMANY, ITALY, SWITZERLAND, AND SPAIN.

A FIVE-MAN NEGOTIATING PANEL HEADED BY FINANCE UNDER-SECRETARY ALFREDO PIO DE RODA JR. WILL LEAVE FRIDAY THIS WEEK FOR TAX TREATY TALKS IN WASHINGTON, D.C.

THE PANEL WILL TRY TO FORGE A BILATERAL AGREEMENT TO PREVENT THE DOUBLE TAXATION OR TAX EVASION ON CORPORATE AND INDIVIDUAL INCOMES OF FILIPINOS IN THE US AND AMERICAN IN THE PHILIPPINES.

THE NEGOTIATIONS WILL FOCUS ON THREE MAJOR AREAS. THESE ARE:

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1. TAXATION OF PROFITS OF SHIPPING AND AIRCRAFT

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FM AMEMBASSY MANILA

TO SECSTATE WASHDC 3032

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COMPANIES,

2. TAX RATES ON ROYALTY PAYMENTS FOR PATENTS OF PRODUCTS
NOT CONSIDERED AS ESSENTIAL TO PHILIPPINE ECONOMIC
DEVELOPMENT.

3. A MUTUAL AGREEMENT PROCEDURE TO RE-EXAMINE THE TAXES
COLLECTED BY BOTH COUNTRIES FOR POSSIBLE REFUNDS IN
CASES OF "OVERCOLLECTION."

PIO DE RODA TOLD BUSINESS DAY THAT THE PHILIPPINES IS
ONE OF THE FEW COUNTRIES THAT TAXES GROSS PHILIPPINES
BILLINGS OF AIRCRAFT AND SHIPPING COMPANIES. A CHARGE
OF 2.5 PER CENT IS MADE ON THESE BILLINGS DUE TO THE
FUTILITY OF GETTING THE NET PROFIT ACCOUNTS ON A GLOBAL
BASIS OF SHIPPING COMPANIES, HE SAID.
HE ADDED THAT THE US WANTS SOLE TAXATION OF THESE PROFITS
AND THE PROFITS OF COMPANIES ENGAGED IN SHIPPING AND AIR-
CRAFT-RELATED ACTIVITIES LIKE CONTAINERIZATION.
HE SAID THAT THE PHILIPPINES CONCLUDED A TAX TREATY WITH
BRITAIN LAST YEAR BY ELIMINATING THESE PROVISIONS IN
THE TREATY AND LETTING THE ISSUE BE RESOLVED BY A MERI-
TIME TREATY BETWEEN THE TWO COUNTRIES.
PIO DE RODA SAID THAT THE PHILIPPINES IS WILLING TO TAX
AT LOWER RATES THE ROYALTY PAYMENTS OF LOCAL COMPANIES'
TO AMERICAN FIRMS FOR PATENTS THAT ARE ESSENTIAL TO
PHILIPPINE ECONOMIC DEVELOPMENT.
THE PHILIPPINE GOVERNMENT NOW TAXES THESE PATENTS AT
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35 PER CENT (FOR CORPORATIONS) AND 30 PER CENT (FOR

INDIVIDUALS).

THE CONCURRENT CUSTOMS COMMISSIONER SAID THAT THE PHILIPPINE GOVERNMENT BASES ITS TAX ON THE CHARACTER OF THE PAYOR OF ROYALTY. "IF IT IS A BOI-REGISTERED ENTERPRISE, THEN THE TAX IS LOWER. WHY SACRIFICE GOVERNMENT REVENUE FOR PATENTS ON THINGS LIKE CHEWING GUM?" HE QUIPPED. "THE US IS STILL INSISTING ON DELINEATION OF CULTURAL AND INDUSTRIAL PATENTS," HE SAID. PIO DE RODA SAID THAT THE MUTUAL AGREEMENT PROCEDURE CENTERS ON THE TIME PERIOD WHEN TAXES CAN BE COLLECTED. UNDER PHILIPPINE LAWS, THE CAPITAL GAINS FROM FIRMS REGISTERED WITH THE BOARD OF INVESTMENTS ARE EXEMPTED FROM TAXATION IF THE SHARES OF STOCK ARE NOT DISPOSED OF WITHIN FIVE YEARS FROM THE DATE THAT THE INVESTMENTS WERE MADE.

"THE AMERICANS WANT THIS PROVISION TO BE OPEN-ENDED," HE SAID.

THE FORTHCOMING TALKS ARE A CONTINUATION OF AN OFF-AND-ON SERIES THAT BEGAN IN 1964.

IN THAT YEAR, THE US SENATE RATIFIED A BILATERAL TAX TREATY WITH RESERVATIONS REGARDING THE TAXATION OF DONATIONS TO CHARITY AND THE TAX DEDUCTABILITY OF THESE DONATIONS.

PIO DE RODA SAID THAT THE ORIGINAL DRAFT HAD NO CHANCE OF BEING PASSED IN THE PHILIPPINE CONGRESS. ITS RATIFICATION BY THE PHILIPPINE SENATE WAS EXPLOYED BUT THE CHANCES WERE ALSO DIM.

IN 1973, BOTH PANELS DECIDED THAT THE SOLUTION WOULD BE A PROTOCOL TO AMEND THE OBJECTIONS TO THE TREATY. WHEN THE PHILIPPINE DELEGATION HAD COME UP WITH ITS VERSION OF A DRAFT PROTOCOL, WHICH THEY HOPED WOULD BE RATIFIED BY THE US LEGISLATURE TOGETHER WITH THE TREATY, A NEW 56-PAGE DRAFT WAS PRESENTED TO THEM BY THE US PANEL. SINCE THEY WERE NOT EMPOWERED TO NEGOTIATE ON THIS NEW DRAFT, MATTERS CAME TO A STANDSTILL.

DURING DISCUSSIONS LAST YEAR, IT WAS AGREED TO DRAW UP ANOTHER DRAFT AND THIS IS WHAT THE FIVE-MAN PANEL WILL BRING TO THE WEEK-LONG TALKS IN WASHINGTON
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